

DDI-453-75

CENTRAL INTELLIGENCE AGENCY
WASHINGTON, D.C. 20505

14 February 1975

MEMORANDUM FOR: Lieutenant General Daniel O. Graham, USA
Director, Defense Intelligence Agency

SUBJECT : Your Comments on "The Measurement and
Meaning of Defense Burden in the Soviet
Setting"

1. Thank you for your thoughtful and well-reasoned comments on our paper on the Soviet defense burden. Your comments will help sharpen and put into perspective the message that we are trying to convey.

2. As you point out, the paper does not consider Soviet political and power aims or the scale of Soviet programs measured in US costs. Its goal is quite different: that of presenting an analysis of the burden from an economic standpoint together with an examination of what we know about how the Soviets view the burden.

3. I agree that the paper might be misinterpreted. Indeed, this seems to have been the case. I believe that this can be corrected, however, and that the paper has a strong and important message. That is, the Soviet economy is capable of sustaining the magnitude and pace of the Soviet defense effort and that the Soviet leaders believe this to be the case. If this message--on which apparently we are in complete agreement--does not come across loud and clear, our exposition is at fault. I shall examine the paper again to make sure that we get this point across.

DIA review(s) completed.

MORI/CDF

4. I intend to distribute a revised unclassified (Official Use Only) version of the paper to a limited number of people working in the Soviet field. I am doing this because I believe we have an important contribution and because I would like to stimulate more dialogue with some key academics on the subject. We shall also include a discussion of the size of Soviet programs in dollar cost terms in the appropriate section of the paper.

5. As you know, we now have a number of projects under way with DoD/Program Analysis and Evaluation regarding the size of the Soviet defense effort and comparing US and Soviet programs. These are being undertaken at the request of the Secretary of Defense. It is my understanding that DIA and CIA are in good communication at the working level in connection with these projects.



EDWARD W. PROCTOR
Deputy Director for Intelligence

STATINTL

Memorandum for Lt. General Graham

Subject: Your Comments on "The Measurement and Meaning
of Defense Burden in the Soviet Setting"

EWProctor:fbr

Distribution:

Original and 1 - Addressee

- 1 - Director/OER with copy of basics
- 1 - Director/OPR with copy of basics
- 1 - Acting Director/OSR with copy of basics
- 1 - OSR [redacted] with copy of basics
- 1 - DDI Chrono with copy of basics
- 1 - DDI DIA File with copy of basics
- 1 - DDI OSR File with copy of basics

STATINTL

*Received this on 7 Feb
passed them to [redacted] on 11 Feb*

STATINTL

MEMORANDUM FOR: D/OER, AD/OSR, D/OPR

Ed Proctor finds this a thoughtful, well-reasoned paper. It broadens the scope of our dialogue on the "burden" question. He would like your advice on:

- 1 - What our initial response to General Graham should be.
- 2 - What we should do with our paper.

May we have your views on the first of these questions on Friday?

Neil

5 Feb 75
(DATE)

FORM NO. 101 REPLACES FORM 10-101
1 AUG 54 WHICH MAY BE USED.

(47)



S-8312/DI-3H

29 JAN 1975

TO: Deputy Director for Intelligence
Central Intelligence Agency
Washington, D. C. 20505

SUBJECT: Comments on CIA Paper, "The Measurement and Meaning of
Defense Burden in the Soviet Setting" (U)

Reference: DIA Memorandum for the Secretary of Defense, 7 January 1975,
subject: Soviet Defense Burden (U).

1. (C) I commented recently, in the reference cited above, on some aspects of the "burden" paper. While I believe that paper is a very useful effort to address a difficult area, I believe that the importance of this subject justifies some additional comments.
2. (C) Although economists are responsible for creating the concept of burden, as you know they are almost universal in denying its usefulness in international economic comparisons. The inherent problem with comparing "burden" rates is the difference in price relationships within each country even when the two countries are producing the same quantities of identical items. You are well aware that distortions occur in both market and controlled economies, and price structures may differ because of:
(a) varying productivity or input costs, (b) arbitrary setting of prices for resources or products, and (c) differences in markets. As the burden paper indicates, the use of factor prices eliminates only "some of the distortions in Soviet pricing."
3. (C) In the Soviet Union and COMECON economies, these distortions are particularly great, and a few major concerns resulting from them are noted below:

a. The measure of burden used in the "burden" paper is, principally, percentage of GNP allocated to the defense sector. The burden paper offers several possible percentages of national aggregates absorbed by the defense sector, but concludes overall that the defense effort for 1972 is probably about 6% of GNP (p. 5) and "less than 8%" (p. 1). Table 1 (p. 5) also shows that, for 1972, the defense shares of U. S. and U.S.S.R. national aggregates was about six percent for each country. There is a possibility, perhaps probability, that non-economists will

Classified by..... DI (DIA)
SUBJECT TO GENERAL DECLASSIFICATION
SCHEDULE OF EXECUTIVE ORDER 11652
AUTOMATICALLY DOWNGRADED AT TWO
YEAR INTERVALS
DECLASSIFIED ON 31 OCTOBER 1983

reason from such comparisons that the Soviet defense effort is substantially smaller than our own, because it absorbs a roughly equal percentage of an economy about one-half the size of ours (as measured in rubles converted to dollars). For that reason, I believe that analyses based on "percentage of GNP" methods convey an inaccurate impression to persons unsophisticated in such analyses.

b. If the data were available, certain adjustments could be made to the rubles to make them more comparable with Western economies. One could add the subsidies provided the defense sector, and the advantages or priorities provided the defense sector in the form of high quality resources or products, and also include the opportunity costs such as the differential wages not paid the military vis a vis the civilians. Even if these adjustments could be made with some accuracy, their inclusion in an analysis undertaken largely from the economic viewpoint may obscure, rather than illuminate, a major consideration. I refer to the fact that, in the Soviet Union, the term "political economy" applies with particular force. The economy is an instrument of state policy, and that policy has consistently been to give the war-supporting industries and defense sector the highest priority. While this memorandum is not the instrument to review the abundant evidence supporting this point, I believe that it is very relevant to a consideration of "burden" to observe that, from the political viewpoint, the relevant question is whether Soviet aims in the arena of comparative national power are being achieved at a cost which the Soviet leadership considers acceptable and sustainable. The historical consistency of Soviet economic policy, the gradual but visible improvements in the Soviet consumer sector, and the lack of effective counter pressures all suggest that defense spending is viewed, against Soviet progress in improving Soviet military power and stature relative to the U. S., as a tolerable burden. The Soviet leadership would, of course, welcome conditions which permitted its aims to be achieved at lower cost.

c. The burden rate measures, in effect, only the economic loss as a portion of the goods produced during a given period, and fails to consider what might have been produced. It could be argued that the U. S. burden rate is overstated at 6 per cent, insofar as this measure fails to consider our tremendous potential to produce, and the under-employment of labor and productive capacity. In contrast, the Soviet defense sector has absorbed critical capital goods which could have accelerated the Soviet economic growth rate. For this reason, one criterion of defense burden which should be examined is the proportion of key products or technologies, rather than industries, devoted to defense. In the area of microelectronics, for example, the Soviets have

not achieved production technologies for mass production and the small amount produced is therefore devoted primarily to defense. As a result, the Soviets provide a very small quantity of calculators and computers to the civil sector and consequently impede its productivity and growth. Viewed in this light, the real cost of defense to the Soviets has been its sacrifice of even higher economic growth rates.

4. (S) All of these difficulties should cause us to reconsider the use of burden and comparative measurements in percentage of GNP. It may be possible to devise more meaningful and communicable comparisons than those used in the burden paper, and also to treat some very significant U.S. - U.S.S.R. economic comparisons. For example, the following statements are, in my opinion, much more meaningful for the general public and as a basis for U. S. defense policy decisions:

a. The Soviet military budget, measured in terms of the equivalent dollar purchasing power, has been higher than that of the U. S. for every year since 1971.

b. The proportion of the Soviet military budget devoted to "military investments" -- that is, to the acquisition of new military hardware and to research and development -- has been approximately double that of the United States for every year since 1971.

c. Recently Soviet military expenditures have been growing at a rate approaching the six percent growth rate of the Soviet economy.

d. Continuation of a higher rate of expenditure and a higher rate of increase in expenditure, while not a perfect reflection of the rate of change in relative military power, indicate a continuing shift toward the Soviet Union in the U.S. - U.S.S.R. military balance.

e. At the conclusion of its present major effort to replace and modernize its land based and submarine based ballistic missile force, the Soviet Union will have the option of reducing military expenditures or accelerating the already impressive rate of modernization and improvement of its general purpose forces. With the strategic force relationship fixed by the SAL treaties, the election of the latter option would accelerate the shift in the military balance toward the Soviet Union.

f. Every leadership elite in the Soviet Union since the October Revolution has regarded the relative economic power of the Soviet Union, measured in terms of war supporting industry, as a principal factor supporting the achievement of Soviet aims.

g. Given this tradition, and the fact that its economy and war supporting industry now permit it to exceed current U. S. spending, in terms of the purchasing power of its military budget, at an acceptable "burden" level, the Soviet leadership can be expected to maintain or increase defense spending unless there are strong incentives or pressures which, in the aggregate, make a reduction advantageous.

h. The economic "burden" of defense spending is not, at this time, visibly influencing the Soviet leadership toward reduced military spending. (Agreed limitations on strategic armaments appear to have been influenced principally by U. S. strategic strength, corresponding fear of nuclear war, and the view that other options were preferable. The fear of nuclear war led Khrushchev, after Soviet studies of the effects of nuclear war, to revise the long standing Soviet doctrine that war between the Soviet Union and the capitalist powers is inevitable. In Khrushchev's formulation, the power of the Soviet Union made the doctrine obsolete, such wars are "no longer fatalistically inevitable," "we have no need of war," can avoid nuclear war, and can "win" by overtaking the United States in industrial output and by supporting "wars of national liberation" and other activities to weaken the Western powers and change the power relationship in favor of the Soviet bloc.)

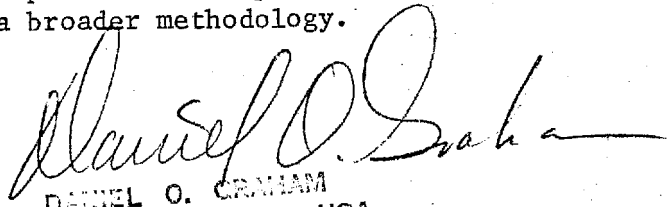
i. Some aspects of present Soviet attitudes are influenced, to some degree, by the fact that Khrushchev's aim "to equal and surpass" the United States in economic power by 1970 has clearly not been achieved, in spite of impressive economic progress. The serious Soviet economic deficiencies lie in agricultural productivity, the variability of annual production of basic cereals, and relative inferiority in high level technology. It is belaboring the obvious to observe that Soviet leaders have perceived detente as, among other things, an opportunity to obtain Western and, particularly, American help in ameliorating these problems. What the Soviet attitude toward detente might be if these problems were substantially solved is, at the very least, a legitimate area for thought and study with respect to future U. S. national security.

5. (S) To sum up an already lengthy memorandum, the role of the Soviet economy in the whole spectrum of Soviet strategy appears to be better defined, more coherent, more political, and more influential than economic considerations in our own country. While I do not hold that each of the underlined statements above is precisely true and correct as stated, I believe that each of them is substantially or "operationally" true and that, in the aggregate, they present a substantially correct picture. That picture is a very different one from that which I believe

the public would get from the "burden" paper, and for that reason I believe that its publication is not in the best interest of the United States.

6. (S) Since DIA's capability for economic studies is limited by our small number of personnel, I do not at this time have a well considered alternative analysis to offer. However, I believe that some or perhaps all of the points raised above should be weighed for incorporation in any paper intended to publicize our Government's views on Soviet military spending and the role of the Soviet economy in Soviet strategic considerations. I understand that CIA has decided to defer publication of the burden paper, and we may now have an opportunity to broaden the analysis to include some of the above points.

7. (C) The analysis of the cumulative U. S. - Soviet investment and inventory levels in relation to the growth in capabilities in the various military missions is now receiving growing attention by the intelligence community at the request of Dr. Marshall, Director of Net Assessment. DIA has participated in initial seminars with the Military Economic Review Panel and representatives of Dr. Marshall's office, as well as CIA, on the matter of inventory valuations as they relate to the measurement of capability. DIA expects to be involved extensively in this project, as the objectives and the definitional or procedural matters are clarified. I believe that at least some of the points underlined in paragraph 4. above should be addressed in this analysis or in a separate, early undertaking. I do not believe, on the other hand, that the method of comparing percentages of GNP and economic burden, without considering Soviet political and power aims, is meaningful. I recommend we move toward a broader methodology.



DANIEL O. GRAHAM
Lieutenant General, USA
Director

OFFICE OF THE DD/I

10 January 1975

NOTE FOR: Director/OER
Acting Director/OSR

Attached is a letter from Danny on the "burden" paper. In this letter Danny urges me not to publish and give it broad dissemination outside the Government.

As you will remember I had some problem with the way some of the material in the paper was presented and asked that it be redone. I want you to continue working on the paper with the objective of making it unclassified and distributable on a broad basis. But, before it is published, I want to review it to minimize the possibility of it being misinterpreted and to maximize its clarity. After I have reviewed the draft, I shall decide whether to publish and shall inform Danny of my decision.

When can I expect to receive a reworked draft?

signed
Ed Proctor

*by given: Walsh
Egan Hoff*

work by 3 Feb ?

ACTION

~~CONFIDENTIAL~~

DDI-76-75



DEFENSE INTELLIGENCE AGENCY

WASHINGTON, D.C. 20301

JAN 7 1975

C-0324/DI

Mr. Edward W. Proctor
Deputy Director for Intelligence
Central Intelligence Agency
Washington, D. C. 20505

Dear Ed:

(C) I note, in your memorandum to the Secretary of Defense, transmitting the paper on the burden of Soviet defense expenditures, your intention to have the paper sanitized so that it can "reach a broad audience outside the Government."

(C) The DIA staff has not yet completed its analysis and review of the paper, but it is already abundantly clear that the issues discussed are very complex. I believe that the conclusions will be properly understood only to the extent that the analytical methodology and its limitations are understood: the paper is therefore useful principally to the sophisticated reader. There is, I believe, a corollary danger that polemicists of various hues can use the paper to suggest conclusions that the analytical method will not support, and thus mislead rather than inform public opinion.

(C) I believe, therefore, that publication of the paper to "reach a broad audience outside the Government" is likely only to feed controversy, and unlikely to serve the public interest. Accordingly, I urge you to refrain from such publication.

(U) The DIA staff is continuing review of the paper, and I expect to provide comments to the Secretary of Defense and to you later this month.

Sincerely,

DANIEL O. GRAHAM
Lieutenant General, USA
Director

~~CONFIDENTIAL~~